ACEC

AMERICAN COUNCIL OF ENGINEERING COMPANIES

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On behalf of the American Council of Engineering Companies

Before the House Committee on Small Business
Subcommittee on Contracting and Infrastructure
hearing on
The Interaction Between the Paycheck Protection Program and Federal Acquisition Rules: What it Means for Government Contractors

Tuesday, March 23, 2021

Chairman Mfume and Ranking Member Salazar:

Thank you for the opportunity to testify before the subcommittee today. It's an honor to represent my firm and my colleagues in the nation's engineering industry to you and the members of the subcommittee.

My name is Robin Greenleaf. I am the CEO of Architectural Engineers, Inc. (AEI), a women-owned engineering firm in Boston, Massachusetts.

I am testifying today on behalf of the American Council of Engineering Companies (ACEC) – the business association of the nation's engineering industry. ACEC member firms drive the design of America's infrastructure and built environment. Founded in 1906, ACEC is a national federation of 52 state and regional organizations representing nearly 5,500 engineering firms and 600,000+ engineers, surveyors, architects, and other specialists nationwide.

More than three-fourths of ACEC members are small businesses.

I am the 2020-21 Chair-elect of ACEC and will have the privilege of serving as the National Chair starting in April. I would also like to note that this is a volunteer position.

Firm Profile

I founded AEI in 1985, and we have been certified by the state of Massachusetts as a women business enterprise (WBE) and disadvantaged business (DBE) since 1986. We also hold WBE/DBE status in Connecticut and Rhode Island.

We have 33 employees. Our professional experience includes heating and air conditioning, plumbing, electrical lighting and power systems, instrumentation, and fire protection engineering. Our project portfolio includes virtually every project type: laboratories, academic facilities, state office, public safety, municipal buildings, airport terminals, courthouses, transportation / infrastructure, commercial high-rise office buildings, corporate headquarters, tenant interiors, residential towers, libraries and museums. Our clients include federal and state agencies, municipalities and towns, and private corporations and owners.

COVID Impacts and PPP Loan

In March of 2020 my state, like so many others, declared a state of emergency due to the pandemic. In mid-March, my firm moved to fully remote operations, and continue to operate remotely today. With 33 employees all doing highly technical work, we committed to providing the same equipment at home as they have in the office to ensure efficiency and seamless transitions no matter where they are located. This was done at significant, unbudgeted expense to the company, but was necessary to maintain operations.

By late March, we had experienced a significant reduction of workload and backlog due to project cancellations and delays, both in our work with our state DOT, airport authorities, and private clients.

In April, we applied for a PPP loan of $590,000, which was approved and funded in late May. This loan allowed us to keep our entire staff on the payroll, even in the face of significant revenue loss, and allowed us some time to regroup our business plan as we adjusted to working remotely.

FAR Credits

Under current federal guidance, forgiven PPP loans will be subject to the “credits” clause of the Federal Acquisition Regulation (FAR 31.201-5).

To understand what is at stake in this approach, it’s important to understand how public agencies negotiate contracts for professional services. An engineering firm’s overhead or indirect cost rate reflects the cost of doing business and includes items such as rent, facilities, equipment, administrative costs, employee fringe benefits, insurance, and other general business costs that are not directly attributable to any specific project or contract. This rate is used in conjunction with direct costs, such as employee salaries, when negotiating contracts with government agencies. These costs are governed by the cost principles in Part 31 of the Federal Acquisition Regulation. They are audited by an outside CPA firm every year and reviewed by the relevant agency. The audited indirect cost rate is used for a one-year accounting period but is also the rate used for the duration of a contract, which is often multi-year.

The most likely implementation of the FAR credit will be a reduction in my firm’s overhead rate to reflect the PPP loan. This is the approach taken in draft guidance presented by the Federal Highway Administration in January and that many State DOTs are adopting as policy.

Summary of Impact to AEI

Approximately 15% of my firm’s work is contracted with public agency clients using a FAR-compliant overhead rate. That includes transit projects administered by the Massachusetts Bay

Transportation Authority (MBTA). We typically contract approximately $900,000 per year with MBTA. In 2021, we expect that revenues from MBTA should stay about the same.

My firm's current overhead rate is 147%. The PPP credit will reduce our rate to about 115%, which will reduce our billings to MBTA and result in a loss of at least $129,000 per year. This is not sustainable and will likely result in our making the business decision to not provide services to clients who request proposals during the impacted time period. MBTA contracts can last for years, and to intentionally incur a loss of this magnitude over a multi-year period is not good business.

Industry Impact

My firm is just one small example. This issue is going to affect thousands of small firms across the country much more dramatically.

When you extrapolate the reduction in billing rates across multiple contracts and multiple clients, it's easy to see how the losses grow significantly. One of our affiliate CPA firms ran the numbers for one of his clients who performs predominantly highway-related work for State DOTs. On a $1.4 million PPP loan, the FAR credit will reduce their rate by 34 points, resulting in a $1.7 million loss in revenue in one year alone and close to $7 million in lost revenue over five years, as most of the DOT work is done under multi-year contracts that lock in the billing rate.

The impact of the credit will fall most heavily on small, minority-owned and women-owned firms that needed the assistance the most and who tend to perform a higher percentage of government contracting. Here are some examples we have collected:

> A WMBE engineering firm with 43 employees in upstate New York received a $826,000 PPP loan. They used the funds primarily to keep employees on the payroll. If they are required to provide a credit to their overhead for loan forgiveness, the firm's overhead rate would drop from 159% to 114%. Based on projected labor in 2021, the firm's revenue would drop from $5.5 million to $4.5 million – *a loss of more than $1 million in annual revenue*.
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> A minority-owned DBE/MBE construction inspection/civil engineering firm with 45 employees in central Ohio received a $770,000 PPP loan. If they are required to provide a credit to their overhead rate for the loan forgiveness, it will reduce their overhead rate from 1.33 to .94. Given their 2021 workload, they will go from a projected $350,000 profit on $4.7 million in revenue to a loss of $298,000, *a total reduction of $648,000*. On multi-year contracts, the impact will be even worse. According to the firm, they would have been better off not accepting the PPP loan and laying staff off.
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> A disadvantaged business and women-owned small business enterprise with 45 employees in southwestern Illinois received a $700,000 PPP loan. If they are required to provide a credit to their overhead rate for the loan forgiveness, it will reduce their overhead from 172% to 137%. Given their workload, they will *lose approximately $690,000 in revenue in the next year*. When the PPP loan came out, they made the choice

to keep their engineering field people employed even though projects were delayed due to COVID, and to upgrade their computer equipment so designers could work from home and still access large files.

Mr. Chairman, according to SBA data we have reviewed, 265 Maryland businesses in the “engineering services” NAICS contracting code received PPP loans larger than $150,000 in 2020. Those firms employ 12,465 people. Not all of those businesses are ACEC members and not all contract with public sector agencies, but it’s a good approximation of the scope of impact in your state.

Congresswoman Salazar, there were 561 “engineering services” businesses in Florida that took PPP loans totaling $357 million in 2020. Those businesses employ more than 25,000 people. Again, not all those companies are the types of firms that contract with the government, but several hundreds of them will be impacted by this issue.

It’s important to note that other contractors working on federal-aid projects for state and local agencies are not subject to these same requirements. While my rates are reduced, other businesses working on the same infrastructure projects have been able to retain the full benefit of the PPP. This uneven treatment does not seem fair.

I’d like to point out several anomalies and inconsistencies between the intent of the PPP loan, and the impact on firms having effectively reimburse government clients because of the interpretation of FAR credit clause:

1. For many ACEC member firms who perform a significant volume of DOT work, the net effect will be that they would be repaying almost their entire loan amounts in the first year following application of their reduced overhead (OH) rate. If these firms had opted to repay the loan, they would have had either two or five years to repay, depending on when the loan was funded.
2. The total value of the PPP loan is being applied as a credit to effectively reduce a firm’s overhead rate for the entire year contractually, yet the PPP loan amount is calculated based on an expected payroll for an 8 or 24 week period, depending on how forgiveness is calculated. There is no discussion of application of the lowered overhead rate only to hourly invoicing which occurred over the same 8 or 24 week period. If the reduced overhead rate is applied to an entire year of contracting, then the double dipping is on the government’s side.
3. The PPP loan funds came from the federal government, yet in many cases, such as my firm, the credit is given to local/state government. This is a one-way flow of funds which puts the local/state government entity in the position of receiving the final benefit.
4. The FAR credit clause is causing the overhead pool to be reduced by the amount that was received under PPP. So, if you received $100,000, that is what is reducing the pool. This credit clause is targeting government contractors who are working on projects being invoiced on an hourly basis. Government contractors who have fixed priced contracts are not impacted by the FAR credit clause, which is unfair treatment, and puts us at a disadvantage with our competitors.

Conclusion

This is government giving with one hand and taking back with the other. Small businesses like mine were experiencing tremendously difficult circumstances and a very uncertain economic outlook as projects were shut down and offices shuttered in the spring of 2020. Ultimately, according to a recent study from our Research Institute, engineering and design services revenue fell an estimated 7% in 2020, significantly underperforming overall construction activity over the period. As you can imagine, the disruption hit our small businesses the hardest. The assistance provided through the PPP enabled those firms to maintain their payroll and meet other expenses during this very turbulent economic period.

Now those small businesses are facing the imposition of a credit for forgiven PPP loans, which will further inhibit their ability to recover and grow. According to our most recent economic forecast, we expect total engineering and design services revenue will decline further in 2021, falling 4% from 2020 levels. The prospect of firms being forced to credit back the critical PPP assistance in this economic environment is daunting.

There's a real sense of urgency in the industry to get this issue resolved. Firms that already received forgiveness are starting the annual audit process and seeing the impact of the credit on their rates. Those that have not yet applied are coming up on the 10-month deadline to start repaying their PPP loans. Banks are pressuring them to decide whether to apply for forgiveness. Our small business owners need to make critical business decisions about the impact on their rates and projected revenues and the employment ramifications.

If unchanged, this policy will create a disincentive for women-owned firms, DBEs, and other small businesses to compete for work for public agencies. It will deprive the government of qualified engineering services, and it will hamper efforts to expand small business and DBE contracting opportunities.

At a time when the industry is very eager to work with you and your colleagues to deliver a robust infrastructure-based economic recovery agenda, the prospects for those opportunities are dimmer because of this credit holding us back.

Congress already made clear that forgiven PPP loans are not to be treated as income for tax purposes and then further clarified in the year-end omnibus bill that covered expenses are deductible. In the same way, Congress ought to make clear that forgiven PPP loans are not income under the FAR. This was emergency relief to support employers, and our businesses ought to be able to take full advantage of the program.

Thank you again for the opportunity to testify.